

Legislative Audit Division

State of Montana



Report to the Legislature

March 1997

Financial-Compliance Audit

For the Fiscal Year Ended June 30, 1996

Department of Environmental Quality

This report contains seven recommendations to improve accounting controls and compliance procedures within the department. These recommendations include:

- ▶ **Reviewing indirect cost rate calculations.**
- ▶ **Recovering operator certification costs.**
- ▶ **Increasing oversight of supply purchases.**
- ▶ **Improving accounting procedures.**

**Direct comments/inquiries to:
Legislative Audit Division
Room 135, State Capitol
PO Box 201705
Helena MT 59620-1705**

FINANCIAL-COMPLIANCE AUDITS

Financial-compliance audits are conducted by the Legislative Audit Division to determine if an agency's financial operations are properly conducted, the financial reports are presented fairly, and the agency has complied with applicable laws and regulations. In performing the audit work, the audit staff uses standards set forth by the American Institute of Certified Public Accountants and the United States General Accounting Office. Financial-compliance audit staff members hold degrees with an emphasis in accounting. Most staff members hold Certified Public Accountant (CPA) certificates.

Government Auditing Standards, the Single Audit Act of 1984 and Amendments of 1996, and OMB Circular A-128 require the auditor to issue certain financial, internal control, and compliance reports. This individual agency audit report is not intended to comply with these reporting requirements and is therefore not intended for distribution to federal grantor agencies. The Legislative Audit Division issues a statewide biennial Single Audit Report which complies with the above reporting requirements. The Single Audit Report for the two fiscal years ended June 30, 1995 has been issued. Copies of the Single Audit Report can be obtained by contacting:

Single Audit Coordinator
Office of Budget and Program Planning
State Capitol
Helena MT 59620
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Deputy Legislative Auditors:
Jim Pellegrini, Performance Audit
James Gillett, Financial-Compliance Audit

March 1997

The Legislative Audit Committee
of the Montana State Legislature:

This is our financial-compliance audit report on the Department of Environmental Quality for the fiscal year ended June 30, 1996. We performed a single year audit to efficiently place this newly established and reorganized department on the audit cycle. Our report contains recommendations concerning indirect cost calculations, water and wastewater operator certification cost recovery, office supply purchasing, accounting procedures and subrecipient monitoring.

We thank the department director and staff for their assistance and cooperation during the audit.

Respectfully submitted,

(Signature on File)

Scott A. Seacat
Legislative Auditor

Legislative Audit Division

Financial-Compliance Audit

For the Fiscal Year Ended June 30, 1996

Department of Environmental Quality

Members of the audit staff involved in this audit were Jody Brandt, John Fine, Tori Hunthausen, Lorry Parriman, and Kris Wilkinson.

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Appointed and Administrative Officials

Department of Environmental Quality

Mark Simonich, Director

Curt Chisholm, Deputy Director

Judy Hanson, Centralized Services Division Administrator

John Arrigo, Enforcement Division Administrator

Jan Sensibaugh, Permitting and Compliance Division Administrator

Van Jamison, Planning, Prevention, and Assistance Division Administrator

Denise Mills, Remediation Division Administrator

Board of Environmental Review

		Term <u>Expires</u>
Cindy Younkin, Chairperson	Bozeman	1998
Daniel Dennehy	Butte	1998
Joe Gerbase	Billings	2000
Paul Hanson	Glendive	1998
Russell Hudson	Libby	2000
Roger Perkins	Laurel	2000
Garon Smith	Missoula	2000

Petroleum Tank Release Compensation Board

		Term <u>Expires</u>
Jean Riley, Executive Director		
Gary Tschache, Chairperson	Bozeman	1997
Diane Savage, Vice Chairperson	Sidney	1997
Gary Basso	Billings	1998
Laura Nordahl	East Helena	1998
Dallas Herron	Kalispell	1998
Mark Simonich, Director, DEQ	Helena	
Bruce Suenram, State Fire Marshall	Helena	

Department of Environmental Quality

This report contains the results of our financial-compliance audit of the Department of Environmental Quality (department) for the fiscal year ended June 30, 1996. The department commenced operations July 1, 1995, so the audit covers its first year of operations. We reviewed the implementation status of several recommendations made to predecessor organizations which administered programs now included in the department. The department implemented all five recommendations directed to its programs in the prior Department of State Lands audit. The department implemented one and partially implemented one of the recommendations directed to its programs in the prior audit of the Department of Health and Environmental Sciences (DHES) for the fiscal year ended June 30, 1995.

Of three issues discussed in the DHES report for the two fiscal years ended June 30, 1994, the department did not take corrective action to comply with federal subrecipient monitoring requirements and state statutory requirements regarding matching funds for local water pollution control facilities projects.

In fiscal year 1995-96, the department recorded all revenue from indirect charges as Federal Indirect Cost Recoveries in the Internal Service Fund. The impact of this error resulted in our qualified opinion on the department's financial schedules on page A-3. Department personnel corrected this error in fiscal year 1996-97.

This report contains seven recommendations. Six recommendations address issues relating to improved compliance with state laws and regulations. The other issue addresses monitoring of subrecipients of federal grant money.

Report Summary

The listing below serves as a means of summarizing the recommendations contained in the report, the department's response thereto, and a reference to the supporting comments.

Recommendation #1 We recommend the department ensure all costs are included in indirect cost calculations. 8

Department Response: Concur. See page B-4.

Recommendation #2 We recommend the department implement procedures to recover all operator costs through licensing and examination fees as required by state law. 8

Department Response: Concur. See page B-4.

Recommendation #3 We recommend the department:

A. Implement procedures to ensure revenue and expenditure accruals are recorded in accordance with state law.

B. Record financial activity for state operations in the proper fund. 11

Department Response: Concur. See page B-4.

Recommendation #4 We recommend the department increase oversight of office supplies purchases to improve compliance with state purchasing policy. 12

Department Response: Concur. See page B-5.

Recommendation #5 We recommend the department ensure the Air Pollution Control Advisory Council operates in accordance with state law. 13

Department Response: Concur. See page B-5.

Recommendation #6 We recommend the department seek legislation amending

Report Summary

current law requiring rules be promulgated only if local
matching funds will be used to finance water pollution
control facilities. 13

Department Response: Concur. See page B-6.

Recommendation #7

We recommend the department implement procedures
to ensure monitoring of grant subrecipients as required
by federal regulations. 14

Department Response: Concur. See page B-6.

Introduction

Introduction

We performed a financial-compliance audit of the Department of Environmental Quality (department) for the fiscal year ended June 30, 1996. The objectives of the audit were to:

1. Determine if the department complied with applicable laws and regulations.
2. Make recommendations for improvement in the management and internal controls of the department.
3. Determine if the department's financial schedules present fairly the results of operations for the fiscal year ended June 30, 1996.
4. Determine the status of audit recommendations from prior audits of entities now administered by the department.

In accordance with section 5-13-307, MCA, we analyzed the cost to implement the recommendations in this report and believe the cost is not significant. Areas of concern regarding compliance with laws and regulations and state accounting policy deemed not to have a significant effect on the successful operation of the department's programs are not specifically included in this report, but have been discussed with management.

We performed procedures to evaluate charges for services for costs incurred in the Internal Service Fund as required by Section 17-8-101(5), MCA, and found the charges and fund equity to be reasonable for the operations in this fund. The issue on page 8 related to certification and licensing costs involves a Special Revenue Fund Account.

Background

The 1995 Legislature created the department as part of a major reorganization of the environmental and natural resources functions of state government. The enabling legislation, Chapter 418, Laws of 1995, assigned functions related to permitting facilities, enforcement of environmental standards and remediation of environmental degradation to the department.

Introduction

The department received the staff, budget resources, and duties of five programs at the former Department of Health and Environmental Sciences: Air Quality, Water Quality, Waste Management, Environmental Remediation, and the Petroleum Tank Release Compensation Board. Also transferred by legislation to the department were the Energy Division of the Department of Natural Resources and Conservation and the Reclamation Division of the former Department of State Lands. Certain Central Services personnel from all three organizations were assigned to the department.

In March 1996, the department initiated an internal reorganization along the functional lines of planning, permitting, enforcement and remediation. Department management obtained budget transfers to reflect financial activity for fiscal year 1995-96 in this program structure. The financial schedules report the department's operations in the restructured divisions.

The Planning, Prevention and Assistance Division develops integrated air, water, waste management, and energy plans to conserve and protect Montana's resources. The division monitors environmental conditions, maintains data on the condition of Montana's environment, encourages businesses and government units to adopt sound environmental practices, and provides technical and financial assistance to implement improved environmental facilities.

The department's Permitting and Compliance Division administers the permitting and compliance activities which relate to various federal and state air and water quality, solid waste, land use and pollution remediation laws. The division reviews and assesses all environmental permit applications, prepares appropriate environmental impact documents and inspects facilities to determine compliance with permit terms and the underlying laws and regulations. Personnel in this division work with facility operators to bring them into compliance when violations are discovered.

Introduction

The Enforcement Division develops policies for thorough and timely enforcement of air quality, water quality, solid waste, hazardous waste, and reclamation laws and regulations and works to attain consistent and predictable application of enforcement policies in all the department's work units. Division personnel coordinate legal and technical aspects of enforcement actions and operate a citizen complaint and information tracking system.

In the Remediation Division, department staff oversee cleanup at state and federal Superfund sites, reclamation of abandoned mines, regulation of underground storage tanks, and removal of sources of groundwater contamination, such as spills of agricultural or industrial chemicals.

The Petroleum Tank Release Compensation Board is attached to the department for administrative purposes. The board is responsible for administering the petroleum tank release cleanup fund. Staff of the board review and process claims for reimbursements to tank owners who have experienced costs due to remediation of contamination from leaking underground storage tanks.

Responsibility for central budgeting, accounting, fiscal reporting, internal auditing, procurement contracts and information technology services rests with the Centralized Services Division. Most of these services are financed in an Internal Service Fund by allocation of costs to the other divisions in the department rather than by direct budgeting and legislative appropriation. Activity of the Director's Office, which includes the department's personnel office and legal unit, is reported as part of Central Management Program on the financial schedules.

Prior Audit Recommendations

Prior Audit Recommendations

Our office performed an audit of the Department of State Lands for the two fiscal years ended June 30, 1995. The report made five recommendations to improve operations now assigned to the Department of Environmental Quality (DEQ). DEQ has implemented all of these recommendations.

In our report on the financial-compliance audit of the Department of Health and Environmental Sciences (DHES) for the fiscal year ended June 30, 1995, we made two recommendations applicable to DEQ operations. DEQ implemented one recommendation and partially implemented the other. For further discussion of revenue accrual inconsistencies and other accounting issues, see page 9.

We also performed follow-up on three issues discussed in the DHES report for the two fiscal years ended June 30, 1994. DEQ has implemented procedures to end access of terminated employees to data processing systems. DEQ did not propose legislation to revise statutes related to matching funds for local water pollution control facilities (see page 13) or implement subrecipient monitoring for federal grants (see page 14).

Findings and Recommendations

State Compliance

The department administers state and federal laws related to water and air quality, solid waste management, disposal of hazardous materials, toxic waste clean-up, energy conservation, major facility siting, and land use planning. In conducting our audit, we tested the department's compliance with selected laws, including those which we believe to have a material impact on the financial operations of the department. The following six sections discuss areas where the department can improve compliance with legal requirements.

Indirect Cost Rate

Federal regulations allow state agencies to receive reimbursement for indirect costs. Indirect costs are costs incurred for common purposes benefitting more than one program, such as information services networks, personnel administration, and accounting. Section 17-3-111, MCA, requires state agencies to recover indirect costs from the federal programs to the fullest extent possible. Recovery of indirect costs from federal sources reduces the state money needed to support federal programs.

In fiscal year 1995-96, the department negotiated an indirect cost rate with the Environmental Protection Agency (EPA) to recover the indirect costs of services provided to EPA funded programs. Department staff calculated the rate using budgeted expenditures of the Centralized Services Division and the Director's Office. The department did not include the correct carry forward expenditure amounts from the previous fiscal year. In addition, we found the department omitted a portion of budgeted expenditures from the calculation. Had the calculation included the proper amounts, we estimate the department could have recovered an additional \$113,464 from EPA for fiscal year 1995-96. Department officials said the omitted expenditures will be recovered in calculations for future periods.

A department official said the department did not revise the indirect cost pool to include increased budgetary authority approved after the initial rate calculations were made. Although the official said the costs can be recovered in the following year, we estimate the error

Findings and Recommendations

cost the state \$286 in lost interest during the fiscal year since state funds had to cover the federal share of the costs.

Recommendation # 1

We recommend the department ensure all costs are included in indirect cost calculations.

Water and Wastewater Operators Licensing

The department oversees certification and licensing of operators of water treatment plants, water distribution systems, and wastewater treatment plants. Section 37-42-304, MCA, directs the department to charge fees which recover the costs associated with the licensing and certification function. The department paid contracted services expenses of \$11,018 connected with the development of certification examination materials from a source not funded by operators fees. As a result, department personnel did not consider these costs when establishing licensing and examination fees for operators.

Department management said the contract costs were paid from an account funded with water connection fees collected by local governments and utilities, the same entities for which most operators work. Department personnel confirmed that these employers pay approximately 75 percent of the annual licensing fees, but said an analysis of fee adequacy had not been performed for three years. Since state law requires that the licensing function be self-supporting, the department should charge all operator costs to the operator licensing account and set fees commensurate with these costs.

Recommendation # 2

We recommend the department implement procedures to recover all operator costs through licensing and examination fees as required by state law.

Findings and Recommendations

Accounting Issues

Section 17-1-102(5), MCA, requires state agencies to show the receipt, use, and disposition of resources in accordance with generally accepted accounting principles. We noted several instances related to revenue accruals, expenditure accruals and Agency Fund activity where the department could improve compliance with this state law.

Revenue Accruals

According to generally accepted accounting principles, revenue should be recorded in governmental funds, such as the General Fund and the Special Revenue Fund, when the amount is measurable and is expected to be available to finance expenditures of the current fiscal period. The following two cases show inconsistent department practices for recording revenue.

- Owners of water supply systems receive a water connection assessment notice from the department in November which is due March 1 of the following year. At June 30, 1996, department personnel had not recorded a receivable or revenue for past due water connection fees. As a result, Special Revenue Fund fee revenue was understated by \$30,055 for fiscal year 1995-96.
- The department collects annual fees for permits to discharge pollutants into surface water. Department personnel recorded receivables and revenue for the estimated amount of these fees due March 1 but not paid by June 30, 1996. In fiscal year 1996-97, the department collected \$29,400 of fees that were not included in the estimate, and recorded current year revenue rather than prior year revenue. If not corrected, this will result in a \$29,400 overstatement of fiscal year 1996-97 fee revenue in the Special Revenue Fund.

Centralized Services Division personnel, stated they do not always receive complete information from divisions administering the fees. A department official indicated development of procedures to obtain timely revenue information and staff training on revenue accruals is necessary.

Expenditure Accruals

Petroleum Tank Release Compensation Board (board) staff review and approve work plans submitted by contractors for corrective action for petroleum storage tank releases. Contractors send

Findings and Recommendations

Applications for Reimbursement to receive payment from the board for work performed on these projects. The board determines whether the site is eligible or ineligible for Petroleum Tank Release Compensation Board funds. We noted department personnel record expenditures when the board approves payment. As a result, expenditures incurred in one fiscal year were not recorded until the following fiscal year. Under state law and generally accepted accounting principles, expenditures should be recorded at the time they are both measurable and can be estimated. At fiscal year-end, the department should accrue expenditures for approved work plans at sites deemed eligible by the board.

Board personnel said section 75-11-309 (4), MCA, states the board shall obligate money for reimbursement of eligible costs of owners and operators in the order that the costs are finally approved by the board. Therefore, personnel believe no obligation exists until the board takes action. In addition, the board seldom reimburses contractors for all costs claimed. We reviewed three Applications for Reimbursement for contractor costs in fiscal year 1994-95 which were recorded as expenditures in fiscal year 1995-96. The billed and paid amounts and percentage of the billed amount actually paid appear in the table below.

Table 1			
Petroleum Tank Release Compensation Board			
<u>Contractor Billings & Approved Payments</u>			
Contractor	Amount	Amount	
<u>Invoices</u>	<u>Requested</u>	<u>Approved</u>	<u>Percentage</u>
#1	\$151,788	\$136,890	90
#2	155,563	140,156	90
#3	20,674	19,099	92
Source: Compiled by the Legislative Audit Division.			

Although the board did not approve the full amount, the table indicates the amount paid can be estimated from past payment history. Since contractors incur the costs on eligible projects for

Findings and Recommendations

which work plans have been approved and amounts paid can be estimated, the department should record estimated liabilities for these expenditures in the year in which they occur.

Agency Fund Activity

Section 17-2-102, MCA, states fiduciary funds are used to account for assets held by state government as an agent for individuals, private organizations, or other governments. We noted two instances where the department recorded donations for specific purposes in the Agency Fund rather than in the Special Revenue Fund.

- The department received \$1,000 from a third party to help pay the cost of a snowmobile emissions study. The department used the money to match federal funds expended for the study, but recorded the donation as property held in trust in the Agency Fund.
- The department received a donation of \$1,100 for clean up of a contaminated site. The majority of the costs of the project were recorded in the Special Revenue Fund. The department recorded the donation and related costs as revenue and expenditures in the Agency Fund. These amounts have been reclassified as additions and reductions to Property Held in Trust in the accompanying financial schedules.

Recommendation #3

We recommend the department:

- A. Implement procedures to ensure revenue and expenditure accruals are recorded in accordance with state law.**
- B. Record financial activity for state operations in the proper fund.**

Findings and Recommendations

Office Supplies

State law gives responsibility to the Department of Administration to set purchasing policy. Administrative Rules of Montana 2.5.301 directs agencies to buy office supply items from the state's Central Stores or through Central Stores term contracts. Agencies may buy supplies directly from the vendors if the vendors price is a publicly advertised price, established catalog price, or a discount price offered to the purchasing agency and is less than the price available from Central Stores. An agency may also purchase supplies directly from vendors if this authority is included in an agreement delegating the authority to do so.

Of 28 office supplies purchases tested, we found seven instances where department personnel purchased supplies from local vendors which were available at a lower price from Central Stores and the department did not have delegated authority to purchase items from other vendors. In these cases, the department did not follow state policy. Personnel involved in the purchases said they were not aware the items were available through Central Stores.

Recommendation #4

We recommend the department increase oversight of office supplies purchases to improve compliance with state purchasing policy.

Air Pollution Control Advisory Council

Section 2-15-2106, MCA, establishes an Air Pollution Control Advisory Council to advise the department on air pollution related issues. Statute specifies individual members of the council will be appointed representing the following vocations: labor, agriculture, manufacturing, fuel industry, physicians, veterinarians, chemical or environmental engineers, meteorologists, conservationists and urban planning consultants. We found the council has not met since June 1991, even though state law requires a minimum of two meetings per year.

Findings and Recommendations

Department management said agency personnel have used ad hoc advisory groups, such as the Clean Air Act Advisory Committee, to obtain public input on air pollution matters. An attempt to eliminate the council as part of reorganization was rejected in the 1995 legislative session. A department official said the governor has been asked to appoint new members to the Air Pollution Control Advisory Council.

Recommendation #5

We recommend the department ensure the Air Pollution Control Advisory Council operates in accordance with state law.

Local Water Pollution Control Facilities Matching Funds

Section 75-5-501, MCA, requires the Board of Environmental Review adopt rules and establish standards for the use of matching funds by local governments in the planning and construction of water pollution control facilities. Despite the mandatory requirement in the law, the board has not adopted rules or established standards for this purpose. A department official said local matching funds have not been needed to secure funding for such construction. In a previous audit of the Department of Health and Environmental Sciences (DHES), we recommended the mandatory requirement to establish rules and standards for matching funds be revised through legislation. The department should seek legislation to require rules only if local match provisions of this section are used.

Recommendation # 6

We recommend the department seek legislation amending current law requiring rules be promulgated only if local matching funds will be used to finance water pollution control facilities.

Findings and Recommendations

Subrecipient Monitoring

The department receives some federal grant funds which it subgrants to other entities. Under federal regulations, the department is responsible for ensuring subrecipients comply with federal requirements and for resolving findings and questioned costs related to the funds it subgrants. Without adequate monitoring of grant contracts, the department lacks assurance subrecipients comply with federal regulations and risks the loss of future federal funding.

In a past audit of the Department of Health and Environmental Sciences, we noted weaknesses in procedures governing monitoring of grant subrecipients. Although the department now has administrative responsibility for many of the same grants, it has not clarified subrecipient monitoring procedures or enhanced its contract database to list all subrecipients required to have audits under federal regulations. Department personnel said reorganization delayed improvement of subrecipient monitoring procedures.

Recommendation # 7

We recommend the department implement procedures to ensure monitoring of grant subrecipients as required by federal regulations.

Independent Auditor's Report & Agency Financial Schedules

LEGISLATIVE AUDIT DIVISION

Scott A. Seacat, Legislative Auditor
John W. Northey, Legal Counsel
Tori Hunthausen, IT & Operations Manager



Deputy Legislative Auditors:
Jim Pellegrini, Performance Audit
James Gillett, Financial-Compliance Audit

INDEPENDENT AUDITOR'S REPORT

The Legislative Audit Committee
of the Montana State Legislature:

We have audited the accompanying financial schedules of the Department of Environmental Quality for the fiscal year ended June 30, 1996, as shown on pages A-5 through A-14. The information contained in these financial schedules is the responsibility of the department's management. Our responsibility is to express an opinion on these financial schedules based on our audit.

We conducted our audit in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial schedules are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosure in the financial schedules. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial schedule presentation. We believe that our audit provides a reasonable basis for our opinion.

As described in note 1, the financial schedules are presented on a comprehensive basis of accounting other than generally accepted accounting principles. The schedules are not intended to be a complete presentation and disclosure of the department's assets, liabilities, and cash flows.

The department records all revenue collected in the Internal Service Fund as Federal Indirect Cost Recoveries. A portion of the indirect cost recoveries in the fund are from state funded programs and should be recorded as Charges for Services. As a result, Federal Indirect Cost Recoveries revenue is overstated and Charges for Services revenue is understated by \$1,023,676 on the Schedule of Total Revenues, Transfers-In & Other Additions in the Internal Service Fund for fiscal year 1995-96.

In our opinion, except for the effects of the matter discussed in paragraph four, the financial schedules referred to above present fairly, in all material respects, the results of operations and changes in fund balances/property held in trust of the Department of Environmental Quality for the fiscal year ended June 30, 1996, in conformity with the basis of accounting described in note 1.

Respectfully submitted,

(Signature on File)

James Gillett, CPA
Deputy Legislative Auditor

January 10, 1997

DEPARTMENT OF ENVIRONMENTAL QUALITY
SCHEDULE OF CHANGES IN FUND BALANCES & PROPERTY HELD IN TRUST
FOR THE FISCAL YEAR ENDED JUNE 30, 1996

	General Fund	Special Revenue Funds	Debt Service Funds	Internal Service Funds	Expendable Trust Funds	Agency Funds
FUND BALANCE: July 1, 1995	\$ 0	\$ 10,160,882	\$ 0	\$ 775,656	\$ 0	
PROPERTY HELD IN TRUST: July 1, 1995						\$ 4,100
ADDITIONS						
Budgeted Revenues & Transfers-In	128,122	27,867,639		1,859,364		
Nonbudgeted Revenues	613,864	1,042,006	612,828		38,550	
Cash Transfers-In		9,971,473			1,241,885	
Prior Year Revenue Adjustments				1,865		
Prior Year Expenditure Adjustments	60,923	368,790				
Direct Entries to Fund Balance ¹	183,470	4,521,213	1,941			
Support From State of Montana	630,210					
Additions to Property Held in Trust						3,155,482
Total Additions	1,616,589	43,771,121	614,769	1,861,229	1,280,435	3,155,482
REDUCTIONS						
Budgeted Expenditures & Transfers-Out	1,616,483	31,043,012		1,928,454		
Nonbudgeted Expenditures & Transfers-Out		5,335,716	598,150	(11,273)	4,853	
Prior Year Expenditure Adjustments				809	13	
Direct Entries to Fund Balance ¹				331,364	1,275,569	
Prior Year Transfer-Out Adjustments		92,385				
Prior Year Revenue Adjustments	106	436,471				
Reductions to Property Held in Trust						17,075
Total Reductions	1,616,589	36,907,584	598,150	2,249,354	1,280,435	17,075
FUND BALANCE: June 30, 1996	\$ 0	\$ 17,024,419	\$ 16,619	\$ 387,531	\$ 0	
PROPERTY HELD IN TRUST: June 30, 1996						\$ 3,142,507

¹ See note 6 on page A-14.

This schedule is prepared from the Statewide Budgeting & Accounting System. Additional information is provided in the notes to the financial schedules beginning on page A-11.

DEPARTMENT OF ENVIRONMENTAL QUALITY
SCHEDULE OF TOTAL REVENUES, TRANSFERS-IN & OTHER ADDITIONS
FOR THE FISCAL YEAR ENDED JUNE 30, 1996

	General Fund	Special Revenue Funds	Debt Service Funds	Internal Service Funds	Expendable Trust Funds	Total
TOTAL REVENUES BY CLASS						
Licenses & Permits	\$ 25,786	\$ 5,496,093				\$ 5,521,879
Charges for Services	102,229	1,370,635	\$ 500,800			1,973,664
Investment Earnings		598,384	103,267		\$ 38,550	740,201
Fines & Forfeits	605,551	5,747				611,298
Federal Indirect Cost Recoveries	6,920			\$ 1,861,229		1,868,149
Sale of Documents & Merchandise		3,240				3,240
Miscellaneous	1,394	704				2,098
Grants, Contracts & Donations		2,001,596				2,001,596
Other Financing Sources		1,653,450	8,761			1,662,211
Federal		17,343,325				17,343,325
Total Revenues	<u>741,880</u>	<u>28,473,174</u>	<u>612,828</u>	<u>1,861,229</u>	<u>38,550</u>	<u>31,727,661</u>
Less: Nonbudgeted Revenues	613,864	1,042,006	612,828		38,550	2,307,248
Prior-Year Revenue Adjustments	(106)	(436,471)		1,865		(434,712)
Actual Budgeted Revenues	128,122	27,867,639		1,859,364		29,855,125
Estimated Revenues	58,400	30,800,469		1,200,000		32,058,869
Budgeted Revenues Over(Under) Estimated	<u>\$ 69,722</u>	<u>\$ (2,932,830)</u>	<u>\$ 0</u>	<u>\$ 659,364</u>	<u>\$ 0</u>	<u>\$ (2,203,744)</u>
BUDGETED REVENUES OVER(UNDER) ESTIMATED BY CLASS						
Licenses & Permits	\$ (8,899)	\$ (807,045)				\$ (815,944)
Charges for Services	78,621	(820,988)				(742,367)
Investment Earnings		(1,199,084)				(1,199,084)
Fines & Forfeits		(44,553)				(44,553)
Federal Indirect Cost Recoveries		(93,715)		\$ 659,364		565,649
Sale of Documents & Merchandise		(3,465)				(3,465)
Grants, Contracts & Donations		372,240				372,240
Other Financing Sources		(11,550)				(11,550)
Federal		(324,670)				(324,670)
Budgeted Revenues Over(Under) Estimated	<u>\$ 69,722</u>	<u>\$ (2,932,830)</u>		<u>\$ 659,364</u>		<u>\$ (2,203,744)</u>

This schedule is prepared from the Statewide Budgeting and Accounting System. Additional information is provided in the notes to the financial schedules beginning on page A-11.

DEPARTMENT OF ENVIRONMENTAL QUALITY								
SCHEDULE OF TOTAL EXPENDITURES, TRANSFERS-OUT & OTHER REDUCTIONS BY OBJECT BY PROGRAM								
FOR THE FISCAL YEAR ENDED JUNE 30, 1996								
PROGRAM EXPENDITURES BY OBJECT	Central Management Program	Petro Tank Release Comp Board	Planning, Prevention & Assistance Division	Enforcement Division	Remediation Division	Permitting & Compliance Division	Prior Year Expenditure Adjustments	Total
Personal Services								
Salaries	\$ 1,118,333	\$ 590,476	\$ 2,576,416	\$ 295,567	\$ 1,413,060	\$ 3,884,032	\$ (100)	\$ 9,877,784
Hourly Wages						488		488
Other Compensation	2,700		114			75		2,889
Employee Benefits	262,041	150,933	623,082	61,856	350,711	954,452	(317)	2,402,758
Personal Services-Other	22,701							22,701
Total	1,405,775	741,409	3,199,612	357,423	1,763,771	4,839,047	(417)	12,306,620
Operating Expenses								
Other Services	283,067	99,627	3,338,975	137,492	7,570,380	1,198,425	(277,414)	12,350,552
Supplies & Materials	86,858	46,680	133,206	11,746	110,600	281,614	(5,211)	665,493
Communications	64,607	34,316	92,682	8,475	67,339	154,133	601	422,153
Travel	16,858	39,777	150,888	10,489	91,501	149,777	260	459,550
Rent	57,938	55,537	113,414	13,395	139,551	277,231	300	657,366
Utilities			8,293	641	3,245	11,526	1,829	25,534
Repair & Maintenance	5,444	1,509	11,574	1,500	6,854	30,010	244	57,135
Other Expenses	42,643	156,138	645,077	73,583	400,728	932,875	888	2,251,932
Total	557,415	433,584	4,494,109	257,321	8,390,198	3,035,591	(278,503)	16,889,715
Equipment and Intangible Assets								
Equipment		8,856	57,917	9,292	4,122	46,603	2,118	128,908
Intangible Assets			470			1,473	624	2,567
Total		8,856	58,387	9,292	4,122	48,076	2,742	131,475
Capital Outlay								
Land & Interest in Land			20,810					20,810
Total			20,810					20,810
Grants								
From State Sources			47,070		16,075		(21,492)	41,653
From Federal Sources			154,796				(2,905)	151,891
From Other Sources						988,635	(83,639)	904,996
Total			201,866		16,075	988,635	(108,036)	1,098,540
Benefits and Claims								
From State Sources		5,437,705						5,437,705

Total			<u>5,437,705</u>					<u>5,437,705</u>	
Transfers									
Accounting Entity Transfers			<u>3,757,885</u>		<u>20,000</u>	<u>92,385</u>		<u>3,870,270</u>	
Total			<u>3,757,885</u>		<u>20,000</u>	<u>92,385</u>		<u>3,870,270</u>	
Debt Service									
Bonds			<u>421,653</u>					<u>421,653</u>	
Leases			<u>2,101</u>					<u>2,101</u>	
Total			<u>423,754</u>					<u>423,754</u>	
Total Program Expenditures	\$	<u>1,963,190</u>	\$ <u>6,621,554</u>	\$ <u>12,156,423</u>	\$ <u>624,036</u>	\$ <u>10,174,166</u>	\$ <u>8,931,349</u>	\$ <u>(291,829)</u>	\$ <u>40,178,889</u>
PROGRAM EXPENDITURES BY FUND									
General Fund	\$	45,991		\$ 897,685	\$ 9,257		\$ 663,550	\$ (60,923)	\$ 1,555,560
Special Revenue Fund		18	\$ 6,621,554	10,655,735	614,779	\$ 10,174,166	8,267,799	(231,728)	36,102,323
Debt Service Fund				598,150					598,150
Internal Service Fund		1,917,181						809	1,917,990
Expendable Trust Fund				<u>4,853</u>				<u>13</u>	<u>4,866</u>
Total Program Expenditures		<u>1,963,190</u>	<u>6,621,554</u>	<u>12,156,423</u>	<u>624,036</u>	<u>10,174,166</u>	<u>8,931,349</u>	<u>(291,829)</u>	<u>40,178,889</u>
Less: Nonbudgeted Expenditures & Transfers-Out		(11,273)		5,270,266		668,452			5,927,445
Prior-Year Expenditure Adjustments			<u>(44,676)</u>					<u>(291,829)</u>	<u>(336,505)</u>
Actual Budgeted Expenditures		1,974,463	6,666,230	6,886,157	624,036	9,505,714	8,931,349		34,587,949
Budget Authority		<u>4,886,690</u>	<u>7,349,858</u>	<u>11,267,264</u>	<u>929,154</u>	<u>10,764,829</u>	<u>9,921,871</u>		<u>45,119,666</u>
Unspent Budget Authority	\$	<u>2,912,227</u>	\$ <u>683,628</u>	\$ <u>4,381,107</u>	\$ <u>305,118</u>	\$ <u>1,259,115</u>	\$ <u>990,522</u>	\$ <u>0</u>	\$ <u>10,531,717</u>
UNSPENT BUDGET AUTHORITY BY FUND									
General Fund	\$	12,985		\$ 21,403	\$ 50,757		\$ 145,743		\$ 230,888
Special Revenue Fund		2,653,420	\$ 683,628	4,359,704	254,361	\$ 1,259,115	844,779		10,055,007
Internal Service Fund		<u>245,822</u>							<u>245,822</u>
Unspent Budget Authority	\$	<u>2,912,227</u>	\$ <u>683,628</u>	\$ <u>4,381,107</u>	\$ <u>305,118</u>	\$ <u>1,259,115</u>	\$ <u>990,522</u>		\$ <u>10,531,717</u>

¹ See note 7 on page A-14.

This schedule is prepared from the Statewide Budgeting and Accounting System. Additional information is provided in the notes to the financial schedules beginning on page A-11.

Notes to the Financial Schedules

For the Fiscal Year Ended June 30, 1996

1. **Summary of Significant Accounting Policies**

Basis of Accounting

The department uses the modified accrual basis of accounting, as defined by state accounting policy, for its Governmental and Fiduciary Funds. In applying the modified accrual basis, the department records:

Revenues when it receives cash or when receipts are measurable and available to pay current period liabilities.

Expenditures for valid obligations when the department incurs the related liability and it is measurable.

State accounting policy also requires the department to record the cost of employees' annual leave and sick leave when used or paid.

The department uses accrual basis accounting for Proprietary Funds. Under the accrual basis, as defined by state accounting policy, the department records revenues in the accounting period earned, if measurable, and records expenses in the period incurred, if measurable.

Expenditures and expenses may include entire budgeted service contracts even though the department received the services in a subsequent fiscal year. Expenditures and expenses may also include goods and equipment ordered with a purchase order before fiscal year-end, but not received as of fiscal year-end.

Basis of Presentation

The financial schedule format is in accordance with the policy of the Legislative Audit Committee. Effective July 1, 1996, the Legislative Audit Committee approved a new financial schedule presentation for inclusion in agency audit reports. The new format includes nonbudgeted revenue and expenditure activity, as well as, prior year revenue and expenditure adjustments for all financial schedules presented. In addition, financial activity for agency funds,

Notes to the Financial Schedules

if any, is included in the Schedule of Changes in Fund Balances & Property Held in Trust.

The financial schedules are prepared from the Statewide Budgeting and Accounting System without adjustment, except for agency funds which are adjusted to reflect the additions and reductions to property held in trust. Accounts are organized in funds according to state law. The department uses the following funds:

Governmental Funds

General Fund - to account for all financial resources except those required to be accounted for in another fund.

Special Revenue Fund - to account for proceeds of specific revenue sources legally restricted to expenditures for specific purposes. Department Special Revenue Funds include federal activity such as Abandoned Mine Lands and Wastewater Treatment Grants and other Environmental Protection Agency, Department of Interior, and Department of Energy grants. State Special Revenue Funds include the petroleum storage tank cleanup, hazardous waste/Comprehensive Environmental Response, Compensation and Liability Act (CERCLA), underground storage tank, leak prevention, reclamation, solid waste management, air quality, public drinking water, abandoned mines, National Pollution Discharge Elimination System (NPDES) permit, Montana Pole remedial action, subdivision plat review, environmental quality protection, and junk vehicle programs.

Debt Service Fund - to account for accumulated resources for the payment of principal and interest on long-term debt. The department uses this fund for state building and energy programs.

Proprietary Funds

Internal Service Fund - to account for providing goods or services to other agencies or departments on a cost-reimbursement basis. The department's Internal Service Fund includes indirect charges assessed against all units of the department by the Central Management Division for providing department-wide support functions and services.

Notes to the Financial Schedules

Fiduciary Funds

Trust and Agency Funds - to account for assets held by the State in a trustee capacity or as an agent for individuals, private organizations, other governments or other funds. Department fiduciary funds include Agency Fund to account for certificates of deposit held for reclamation projects and Expendable Trust Fund to account for the Rock Creek Trust Fund.

2. **Annual and Sick Leave**

Employees at the department accumulate both annual and sick leave. The department pays employees for 100 percent of unused annual and Fair Labor Standards Act (compensatory) leave credits and 25 percent of unused sick leave credits upon termination. Accumulated unpaid liabilities for annual, compensatory, and sick leave are not reflected in the accompanying financial schedules. In the Proprietary Funds, the increase in annual and compensatory leave liability and 25 percent of the increase in sick leave are recognized as nonbudgeted expenses when the related liability is recorded at year end. The department makes expenditures for termination pay in its annual operational costs. At June 30, 1996, the department had a liability of \$920,716 for annual leave, \$38,041 for compensatory leave, and \$487,255 for sick leave.

3. **Pension Plan**

Employees are covered by the Montana Public Employees' Retirement System (PERS). The department's contribution to PERS was \$704,150 in fiscal year 1995-96.

4. **Fund Balances**

The General Fund is a statewide fund. Each agency does not have a separate General Fund since its only authority is to pay obligations from the statewide General Fund within their appropriation limits. Thus, on an agency's schedules, the General Fund beginning and ending fund balance will always be zero.

The July 1, 1995 fund balances/property held in trust are balances from the former Department of Health and Environmental Sciences. Further discussion of the reorganization is in note 5.

Notes to the Financial Schedules

5. **Reorganization**
- The 1995 Legislature created the department as part of a major reorganization of the environmental and natural resources functions of state government. The department received budget resources of five programs at the former Department of Health and Environmental Sciences: Air Quality, Water Quality, Waste Management, Environmental Remediation, and the Petroleum Tank Release Compensation Board. Also transferred by legislation to the department were the Energy Division of the Department of Natural Resources and Conservation and the Reclamation Division of the former Department of State Lands. Certain Central Services personnel from all three organizations were assigned to the department. As a result, the department's biennium budget reflected the program units which were in other departments in the previous biennium. In March 1996, the department initiated an internal reorganization along the functional lines of planning, permitting, enforcement, remediation, and centralized services. Department management obtained budget transfers to reflect financial activity for fiscal year 1995-96 in this program structure. The financial schedules presented report the department's operations in the restructured divisions, which also include the Centralized Management Program and the administratively attached Petroleum Tank Release Compensation Board.
6. **Direct Entries to Fund Balance**
- The large direct entries to fund balance in the Special Revenue Fund relate to energy and reclamation programs moved to the department from the Department of Natural Resources and Conservation and the former Department of State Lands, respectively, during the reorganization of state agencies. In the Internal Service Fund the direct entries to fund balance relate to the portion of centralized services moved to the Department of Public Health and Human Services during the reorganization of state agencies. The transfer of the Rock Creek Trust Fund assets to a private organization for management generated \$1,275,569 in direct entries to fund balances in the Expendable Trust Fund.
7. **Prior Year Expenditure Adjustments**
- The prior year expenditure adjustments recorded in this column relate to appropriations for programs eliminated during reorganization.

Agency Response

DEPARTMENT OF ENVIRONMENTAL QUALITY

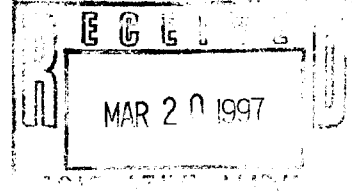


MARC RACICOT
GOVERNOR

MARK A. SIMONICH
DIRECTOR

STATE OF MONTANA

March 17, 1997



Mr. Scott A. Seacat
Legislative Auditor
Office of the Legislative Auditor
State Capitol
Helena, Montana 59620-1705

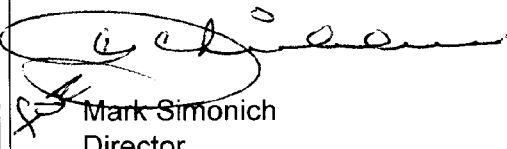
Dear Mr. Seacat:

By this letter, I am transmitting the Department of Environmental Quality's formal response to your Fiscal-Compliance Audit for the fiscal year ending June 30, 1996.

I would like to personally thank your office and the audit staff that was assigned to this endeavor for their dedication and professionalism throughout the course of this audit. Their findings and subsequent recommendations have provided a valuable service and insight to department management relative to our fiscal-compliance responsibilities.

I will be available, along with appropriate staff, for the next meeting of the Legislative Audit Committee.

Sincerely,


Mark Simonich
Director

cc: Judy Hanson, Administrator
Centralized Services Division
MS:JH:jm\seacat96.jh

**DEPARTMENT OF ENVIRONMENTAL QUALITY
RESPONSES TO FISCAL-COMPLIANCE AUDIT
FOR FISCAL YEAR ENDED JUNE 30, 1996**

Recommendation #1

We recommend the department ensure all costs are included in indirect cost calculations.

Response

Concur

The error that was made when negotiating the FY 96 indirect rate was an omission of spending authority transferred from the Department of Public Health and Human Services to the Department of Environmental Quality. The calculation of future indirect rates will include all projected costs to be incurred by the DEQ.

Recommendation #2

We recommend the department implement procedures to recover all operator costs through licensing and examination fees as required by state law.

Concur

The Department of Environmental Quality has proposed rules to increase some of the operator certification fees. The proposed rule amendments were filed with the Secretary of State on March 10th. The publication date and effective date of the increased fees is April 25, 1997.

Examination fees are increasing from \$5.00 to \$20.00. This will increase the revenue so that future expenses associated with development of examination materials will be paid by the water and wastewater operator fees. Late fees are increasing from \$10.00 to \$30.00. This will assist with covering the costs of the program.

Recommendation #3

We recommend the department:

- A. Implement procedures to ensure revenue and expenditure accruals are recorded in accordance with state law.
- B. Record financial activity for state operations in the proper fund.

Response

A. Concur

Revenue accruals. Agency staff from the Centralized Services Division and staff from the program divisions will work together to assure that revenue will be recorded in the proper fiscal year.

Expenditure Accruals. The Petroleum Tank Release Compensation board (board staff) will estimate expenditure liabilities of reimbursement claims on petroleum release sites that have been deemed “eligible releases on eligible sites” that have been received by the board staff but that have not been paid as of June 30. The department Centralized Services Division staff will accrue those liabilities based on the information provided by the board staff.

B. Concur

When the department receives donations for specific state operations, the revenue and expenses will be recorded in the appropriate fund type. The department will also take the necessary steps to obtain the appropriate spending authority or approval to expend the donations.

Recommendation #4

We recommend the department increase oversight of office supplies purchases to improve compliance with state purchasing policy.

Response

Concur

The Central Services Division staff will work with program division staff to assure that the purchasing of supplies will comply with state purchasing policy.

Recommendation #5

We recommend the department ensure the Air Pollution Control Advisory Council operates in accordance with state law.

Response

Concur

Members of the Air Pollution Control Advisory Council (APCAC) serve “at the pleasure of the Governor”. Existing members constitute the APCAC until they resign or are asked to leave the APCAC by the Governor. None of the APCAC’s members have resigned nor have they been asked to resign. Thus, the APCAC is formally in place, though it has been extremely

inactive.

Recently, the Department of Environmental Quality and the Governor's Office contacted most of the members of the APCAC to determine each individual's willingness to continue to serve on the APCAC. The department has prepared a list of potential nominees based on the members' responses, interest expressed by others in becoming involved in the APCAC and recommendations given to us for future APCAC members. This list of possible nominees will be forwarded to the Governor for his consideration. A new APCAC will be appointed soon to replace the current one.

Recommendation #6

We recommend the department seek legislation amending current law requiring rules be promulgated only if local matching funds will be used to finance water pollution control facilities.

Response

Concur

The department will submit legislation to the next legislative session to remove the provision for matching funds for construction of water pollution control facilities. A small amount of federal funds remain available to the state, which the department uses to provide grant funds to small, needy communities for engineering studies. The department currently is under a September 1998 deadline to spend these remaining funds, after which time no further grants will be made.

Recommendation #7

We recommend the department implement procedures to ensure monitoring of grant subrecipients as required by federal regulations.

Response

Concur

The department will develop and implement procedures to ensure subrecipient monitoring of grant subrecipients is conducted as required by federal regulations applicable to grants made by the department.